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In the Supreme Court of the United States

OCTOBER TERM, 1937

No. 505

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

GEORGE W. ELKINS

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 87–100) is reported at 33 B. T. A. 127. The opinion of the Circuit Court of Appeals (R. 387–392) is reported at 91 F. (2d) 534.

JURISDICTION

The judgment of the Circuit Court of Appeals for the Third Circuit was entered July 21, 1937 (R. 392–393). The petition for certiorari was filed October 14, 1937, and was granted November 8, 1937. The jurisdiction of this Court is invoked

under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

The taxpayer received dividends upon capital stock in certain British corporations. Such dividends were declared and paid either "less tax" or "free of tax." The dividend warrants were accompanied in each instance by certificates required by British law, certifying that all British and United Kingdom income taxes due on the profits of the company of which the dividends formed a portion had been paid or would be paid by the corporation to the proper officer for the receipt of taxes. The certificate further indicated that the dividend payment was equivalent to a gross dividend less income tax "appropriate thereto" at the current rate in the case of a dividend "free of tax," or that the warrant represented the net amount of a gross dividend less income tax "appropriate thereto" at the current rate in the case of a dividend "less tax."

1. The principal question is whether the amounts shown on the certificates accompanying dividend payments as taxes "appropriate to" such dividends may be taken as a credit against the Federal income tax as income taxes paid or accrued to a foreign country within the meaning of Section 131 (a) of the Revenue Act of 1928, subject to the limitation imposed by Section 131 (b), and whether any balance not available as a credit may be de-

ducted from gross income under Section 23 (c) of that Act.[1]

STATUTE INVOLVED

The pertinent portions of the statute involved are printed in the Appendix, *infra*, pp. 50–53.

STATEMENT

Throughout the year 1931 the taxpayer, George W. Elkins, a citizen of the United States, owned certain ordinary shares of capital stock in British-American Tobacco Company, Limited, Tobacco Securities Trust Company, Limited, and The Imperial Tobacco Company (of Great Britain and Ireland), Limited. He also owned certain shares of deferred stock in Tobacco Securities Trust Company, Limited. These companies are all corporations organized and existing under the laws of Great Britain, with their head offices in England. (R. 16.)

During the calendar year 1931 these corporations declared and paid cash dividends upon their outstanding stock of the classes noted above. The rates of such dividends and dates of payment are given in detail in the record, pp. 17–20. The dividends on British-American Tobacco Company

[1] A cognate question, not specifically treated by the court below, is whether the amounts shown as taxes "appropriate to" such dividends should be added to the net income actually received as dividends in determining the amount of gross income. If they should be held to be taxes paid by the respondent, they obviously should be included in his gross income.

stock and on The Imperial Tobacco Company stock were paid "free of Income Tax," "free of British Income Tax," or "free of United Kingdom Income Tax," and the dividends on stock in Tobacco Securities Trust Company were paid "less British Income Tax" or "less United Kingdom Income Tax." (R. 17–20, 25, 29, 33, 37, 41, 45, 53, 61.) By communications transmitted to their shareholders at the time the dividend warrants were transmitted the above companies certified to their shareholders that British income taxes and United Kingdom income taxes on the profits of the company of which the dividends formed a part had been paid or would be paid by the company to the proper officer for the receipt of taxes (R. 17–20). The certificates transmitted to their shareholders by British-American Tobacco Company and The Imperial Tobacco Company indicated the dividend paid was equivalent to a gross dividend of a stated amount less the amount of income tax "appropriate to" the gross dividend (R. 25–39, 53–67). The certificates transmitted to its shareholders by the Tobacco Securities Trust Company indicated a gross dividend of a stated amount, less income tax "appropriate to" such gross dividend, and the net amount for which the voucher was issued (R. 41–47).

The net amounts received during the year by the taxpayer as dividends on such shares of stock, stated in terms of United States money, the amounts certified as British and Dominion income taxes "appropriate thereto," and the aggregate of

these amounts, treated as the gross dividends, were as follows (R. 17–20):

Corporation	Net dividend received	Amount shown as tax "appropriate thereto"	Amount shown as gross dividend
British-American Tobacco Company, Ltd.	[1] £12,338.25	$3,743.98	$16,082.[illegible]
Tobacco Securities Trust Company, Ltd.	817.03	201.27	1,018.30
The Imperial Tobacco Company, Ltd.	10,838.44	3,071.86	13,910.30
Totals	23,993.72	7,017.11	31,010.83

[1] These figures are computed at the rate of exchange prevailing at the time of each distribution.

It is the amount shown above as taxes "appropriate to" the dividends received by the taxpayer which gives rise to the present controversy.[1] In addition to this amount the taxpayer paid a surtax of $2,189.91 to Great Britain which is not in controversy (R. 21–22, 73–75, 89).

In his income tax return for 1931 the taxpayer included in gross income, as dividends received from the above foreign corporations, the sum of $31,010.83, being the total amount of cash received as dividends plus the amounts certified as British and United Kingdom income taxes "appropriate thereto" (R. 22, 77). He claimed the above amounts of $7,017.11 and $2,189.91 as a credit under Section 131 (a) of the Revenue Act of 1928 against his Federal income tax, subject to the limitations imposed upon such credit by Section 131

[1] In its opinion the Circuit Court of Appeals erroneously states that the dividend payments were "accompanied by certification that $7,017.11 had been deducted and paid directly to the British Government" (R. 387).

(b), and the balance not allowable as a credit was claimed as a deduction from income under Section 23 (c) of the Act. These provisions are printed in the Appendix, *infra*, pp. 50–53. The amount actually claimed as a credit under Section 131 (a), *supra*, was $5,044.99, and the balance of $4,162.03 was deducted from gross income under Section 23 (c) of the Act (R. 23, 77, 83–85).

The taxpayer kept his books of account and made his income tax returns upon the basis of cash receipts and disbursements (R. 91).

In auditing the taxpayer's return for 1931 the Commissioner of Internal Revenue eliminated from gross income the sum of $7,017.11 certified as British and United Kingdom income taxes "appropriate to" the dividends received from British corporations. He also disallowed the credit of $5,044.99 for taxes paid to a foreign government and disallowed the deduction of $4,162.03 from gross income as taxes paid to a foreign government and not allowable as a credit under Section 131 of the 1928 Act. (R. 11–14, 23.) At the trial before the Board of Tax Appeals the Commissioner conceded that the amount of $2,189.91 paid as surtax to Great Britain was a proper credit against the taxpayer's Federal income tax, leaving for consideration only the questions whether the $7,017.11 certified as British and United Kingdom income taxes "appropriate to" the dividends should be added to the amount actually received as dividends

in determining the amount of the taxpayer's gross income, and whether that amount represented taxes paid to a foreign government within the meaning of Section 131 (a) of the 1928 Act which could be claimed as a credit against the taxpayer's Federal income tax for 1931. The Board of Tax Appeals, in an opinion disposing of this and four other appeals, including an appeal by Mary Duke Biddle, involving the same questions, sustained the Commissioner's determination on both issues. The Circuit Court of Appeals for the Second Circuit, in an opinion filed December 7, 1936, affirmed the decision of the Board in the *Biddle* case, 86 F. (2d) 718. In its opinion in this case (R. 387–392) the Circuit Court of Appeals for the Third Circuit reversed the decision of the Board. Certiorari has been granted in both cases to resolve the conflict of the decision below with the decision in the *Biddle* case, which is No. 55, present Term.

SPECIFICATION OF ERRORS TO BE URGED

The court below erred:

1. In holding and deciding that the sums aggregating $7,017.11 treated for the purposes of British income tax law as taxes "appropriate to" dividends received by the taxpayer upon shares of stock in British corporations constitute gross income to the taxpayer.

2. In holding and deciding that the above sums, aggregating $7,017.11, constitute income, war-

profits, and excess-profits taxes within the meaning of Section 131 (a) of the Revenue Act of 1928.

3. In holding and deciding that the above sums, aggregating $7,017.11, were "paid or accrued during the taxable year to any foreign country" within the meaning of Section 131 (a) of the Revenue Act of 1928.

4. In holding and deciding that the taxpayer is entitled to credit the above sums, aggregating $7,017.11, against his Federal income tax for 1931, subject to the limitations of Section 131 (b), and in holding and deciding that he is entitled to deduct the excess of that credit from gross income under Section 23 (c) of the Revenue Act of 1928.

5. In holding and deciding that the above sums, aggregating $7,017.11, represent income taxes paid to the British Government by the corporations and borne directly by the taxpayer.

6. In reversing the decision of the Board of Tax Appeals.

SUMMARY OF ARGUMENT

The burden is upon the respondent to prove that the amount claimed as a credit constituted income, war-profits, or excess-profits "taxes" within the meaning of the applicable provisions of our revenue acts, and that they were "paid" to a foreign country during the taxable year. The evidence clearly shows that the amounts in question were certified as taxes "appropriate to" the dividends received by the respondent in accordance with requirements of British law; that there was no tax imposed upon the respondent by Great Britain on account of the receipt of such dividends; that such amounts were not imposed upon the respondent or any other person as a tax; that they were not paid to the Crown, either by the respondent or by the dividend-paying corporations; and that the only tax paid to the Crown (except a surtax paid directly to the Crown by the respondent on his dividend income, which is not in controversy here) was the tax at the "standard" rate which was imposed upon and paid by the companies upon their earnings. The amount of the taxes imposed upon and collected from the corporations had no necessary relationship to the amounts certified as income taxes "appropriate to" the dividend payments; the taxes were not paid by the corporations as agents to their shareholders; and if properly allowable as a credit or deduction, they would be

allowable to the corporations rather than to their shareholders. Moreover, though the credit permitted by our statute is for foreign taxes paid by the taxpayer during the taxpayer's taxable year, it does not appear when the corporations paid the tax on the profits here distributed as dividends, even if that tax could be considered as paid on behalf of the stockholders.

The fact that the shareholder of a corporation, domestic or foreign, may, because of his relationship to the corporation as a shareholder, ultimately bear the burden of a tax imposed upon and collected from the corporation does not entitle him to a credit or deduction under our statutes for taxes paid.

The question is not one of construction of our statutes, which are clear and unambiguous, but is a question of applying our statutes to the facts proved. There has been no administrative interpretation of our statutes which justifies the decision below. The Bureau rulings relied upon by the court below are erroneous determinations of fact with respect to the character of taxes imposed under British law. Furthermore, if considered administrative interpretations of our statutes, they are not binding upon the courts if clearly contrary to law or not in accordance with law.

ARGUMENT

I

THE COURT BELOW ERRED IN PERMITTING CREDIT AGAINST FEDERAL INCOME TAX FOR TAXES "APPROPRIATE TO" DIVIDENDS RECEIVED BY THE TAXPAYER

(a) *General Statement*

Section 131 (a) of the Revenue Act of 1928, under which the taxpayer claims the right to a credit against his Federal income tax, provides that in the case of citizens and domestic corporations of the United States the income tax imposed by the Act shall be credited with "the amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country." The amount of this credit is limited by subsection (b) to that "proportion of the tax * * * against which such credit is taken, which the taxpayer's net income * * * from sources without the United States bears to his entire net income" for the year. Any amount of such taxes paid to any foreign country in excess of this limitation is allowed as a deduction from gross income by Section 23 (c) of the Act as "taxes paid or accrued within the taxable year."

In reversing the decision of the Board of Tax Appeals, the court below held that the taxpayer is entitled to a credit under Section 131 (a), *supra*, against his Federal income tax, subject to the limitation of subsection (b) of that section, for the

amount shown on certificates accompanying his dividend warrants as British and United Kingdom income taxes "appropriate to" the dividends received, and that he is entitled to deduct the balance from his gross income for the year as taxes paid or accrued within the taxable year. In so holding the court below reached a conclusion contrary to that reached by the Circuit Court of Appeals for the Second Circuit in *Biddle* v. *Commissioner,* 86 F. (2d) 718, certiorari granted, No. 55, present Term, and *F. W. Woolworth Co.* v. *United States,* 91 F. (2d) 973, now pending on petition for a writ of certiorari, No. 568, present Term. In so holding we submit the court erred.

The deduction from gross income for taxes paid or accrued, like other deduction from gross income, depends upon statutory authorization. Likewise, any credit against the Federal income tax depends upon statutory authorization. In both cases the burden is upon the taxpayer to show facts which entitle him to the deduction or credit claimed. Cf. *Burnet* v. *Houston,* 283 U. S. 223, 227–228; *Welch* v. *Helvering,* 290 U. S. 111, 115.

The taxpayer claimed the credit and deduction as a payment—not as an accrual—of taxes. The burden was therefore upon him to show that he "paid" the $7,017.11 in order to satisfy one of the statutory conditions upon which the credit and deductions are allowed. The burden was also upon

him, as a further condition to the allowance of the credit, to prove that the payment constituted a payment of "income, war-profits, and excess-profits taxes," and to show that such taxes were paid "to a foreign country," "during the taxable year."

The taxpayer does not claim the credit and deduction as a direct payment of taxes, but contends that payment of taxes was made by deduction from dividends paid to him. The taxpayer's argument that the amount involved was paid as taxes by deduction is based upon certain provisions of the British income tax laws and the administrative practice under those laws. The British law has to be proved, just as any other fact. *Ennis* v. *Smith*, 14 How. 399, 426. In his attempt to prove payment of taxes by deduction the taxpayer, in addition to the agreed statement of facts and supporting documents filed with the Board (R. 16–86), introduced in evidence the British Income Tax Act of 1918, which is the basic law in effect in Great Britain today, together with the annual Finance Acts for 1919 to 1932, inclusive,[2] supplemented by the testimony of a witness who qualified as an expert on British income tax law (R. 110–184). This was an appropriate means of proving the British law. *Slater* v. *Mexican National R. R. Co.*, 194 U. S. 120, 130; *In re International Mahogany Co.*, 147 Fed. 147, 149 (C. C. A. 2d); *The Asiatic Prince*,

[2] Original copies of these Acts, obtained from the King's Printer in London, are bound separately and filed as Appendix A to the record.

108 Fed. 287, 289 (C. C. A. 2d); *Ennis* v. *Smith, supra.* The Board of Tax Appeals, after making certain findings with respect to the British law (R. 91–95), denied the credit and deduction claimed.

In so far as the present controversy is concerned, the law of Great Britain is material only in so far as it discloses the actual facts concerning the character of the alleged "tax" and whether it was "paid," as that term is used in our statutes, "to any foreign country." The evidence clearly shows that the amount in controversy does not meet the requirements of the credit and deduction provisions of our statutes.

As a matter of history, the British income tax was first enacted in 1799. This act was based upon the principle of direct assessment, but proved to be unsatisfactory. In 1803 a new act was adopted, which lasted three years. This act was based upon the principle of taxing income at the source. The structure of the Act of 1803 was reproduced in the Act of 1806, and again for another term of five years in the Act of 1811. No new income tax was thereafter reenacted until 1842 (R. 135–136).

The Act of 1842 adopted the model and most of the text of the Act of 1806. The tax was thereafter continued by annual reenactments until the Income Tax Act of 1918 was adopted (R. 135–136).

The Income Tax Act of 1918, 8 & 9 Geo. 5, c. 40, consolidated the provisions of law then in force

and all existing laws relating to income tax were repealed.[3] The 1918 Act is also based upon the principle of collection at the source, and about 70 per centum of the income received by individuals is taxed at the source (R. 123–124).

The tax for each year since 1918 has been imposed by the annual Finance Act, but the imposition, assessment, levy, and collection is governed by the Income Tax Act of 1918 as amended and amplified by the Finance Acts for subsequent years (R. 112–113).

Section 1 of the Income Tax Act of 1918 imposed an income tax upon individuals and corporations. Section 4 imposed a super-tax upon incomes of individuals over and above a stated amount.[4] By Section 38 of the Finance Act of 1927, 17 & 18 Geo. 5, c. 10, the super-tax provisions were amended so that now all income is taxed at a standard rate, and in the case of an individual whose income exceeds a stated amount, a surtax is charged.[5] Corporations are taxed only at the standard rate, which is applicable to individuals and corporations alike (R. 124, 178).

Under the arrangement of the Income Tax Act of 1918 the properties, profits, and gains upon which income tax is charged are classified under

[3] R. 111, 137; Appendix A, Petitioner's Exhibit No. 1.
[4] Record, Appendix A, Petitioner's Exhibit No. 1, pp. 1, 2.
[5] R. 132–133, 178; Appendix A, Petitioner's Exhibit No. 10, p. 28.

five Schedules according to the source of the income. Each Schedule is followed by certain rules for estimating the amount of tax payable upon that particular class of income or property. General rules applicable to all given Schedules are added.

The Schedules under which the amount of tax is estimated are as follows:[6]

Schedule A—Tax on annual value of property in land and buildings.

Schedule B—Tax with respect to occupation of land and buildings.

Schedule C—Tax on income from government securities.

Schedule D—Tax on annual profits and gains from property, trade, or business.

Schedule E—Tax on income from public office, annuities, and pensions.

Many of the rules prescribed for estimating the amount of tax to be paid under these Schedules are highly artificial and have little relation to our concept of income for Federal income tax purposes.[7] The artificial nature of these rules is largely responsible for the present controversy.

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[6] Record, Appendix A, Petitioner's Exhibit No. 1, pp. 147–200.

[7] For instance, the Circuit Court of Appeals for the Second Circuit recently held that the tax paid under Schedule A is not an income tax. *F. W. Woolworth Co.* v. *United States*, 91 F. (2d) 973, affirming 15 F. Supp. 679, No. 568, present Term.

Rule 1 of the General Rules applicable to Schedules A, B, C, D, and E provides: [8]

> Every body of persons shall be chargeable to tax in like manner as any person is chargeable under the provisions of this Act.

Section 237 of the 1918 Act provides that "body of persons" means, *inter alia*, "any company." [9]

The British corporations from which the taxpayer received dividends during 1931 were subject to tax each year under the Act of 1918 as amended by the finance acts. The record does not disclose the nature or extent of their property or profits, or the Schedules under which they were taxed, or the year or years in which the profits distributed as dividends in 1931 were taxed. Clearly, however, they were subject to tax under Schedule D upon the gains and profits, if any, derived each year from their trade or business.

Rule 20 of the General Rules applicable to Schedules A, B, C, D, and E provides: [10]

> The profits or gains to be charged on any body of persons shall be computed in accordance with the provisions of this Act on the

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[8] Record, Appendix A, Petitioner's Exhibit No. 1, p. 194.

[9] Record, Appendix A, Petitioner's Exhibit No. 1, p. 143.

[10] Record, Appendix A, Petitioner's Exhibit No. 1, p. 199. This Rule was based upon Section 54 of the Act of 1842 (R. 151–152). See, also, Rules 19 and 21 (Appendix A, Petitioner's Exhibit No. 1, pp. 198, 199), relating to the payment of any interest or annuity out of profits charged with tax under Schedule D and interest or annuities subject to tax under Schedule D.

> full amount of the same before any dividend thereof is made in respect of any share, right or title thereto, and the body of persons paying such dividend shall be entitled to deduct the tax appropriate thereto.

The tax "appropriate to" a dividend payment is determined on the basis of the standard rate of tax in effect at the time the dividend is declared, regardless of the rate at which the amount distributed was taxed to the company when it was received as income by the company.[11]

Section 33 of the Finance Act of 1924, 14 & 15 Geo. 5, c. 21,[12] requires that every warrant or check drawn by any company after November 30, 1924, in payment of any dividend or interest distributed by the company shall have annexed thereto or be accompanied by a written statement showing:

> (a) the gross amount which, after deduction of the income tax appropriate thereto, corresponds to the net amount actually paid; and
> (b) the rate and the amount of income tax appropriate to such gross amount; and
> (c) the net amount actually paid.

It was pursuant to this requirement that certificates were transmitted to the taxpayer showing the information set out above.

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[11] *Neumann* v. *Commissioners of Inland Revenue*, 18 British Tax Cases 332, 359–361. Printed in record, pp. 297, 324–326.

[12] R. 115–116; Appendix A, Petitioner's Exhibit No. 7, p. 19.

Rule 20, *supra,* is permissive, but the certificate required by Section 33 of the Finance Act of 1924, *supra,* must be furnished in every case. It was under the authority of this Rule that Tobacco Securities Trust Company purported to deduct from its "gross" dividend the amounts certified to be United Kingdom and Dominion income taxes "appropriate to" the dividends. The dividends paid by the other companies being paid "free of tax," the certificates did not purport to show a deduction of tax from the gross dividend, but indicated the amount of income tax "appropriate to" a gross dividend which gave the shareholders the same net return. All of the certificates furnished the information required by Section 33 of the Finance Act of 1924, *supra.* The only amount distributed by the corporation was the cash actually paid to its stockholders.

The amounts certified as taxes "appropriate to" the dividend payments were not paid to the Crown as taxes on the dividends. They relate to amounts paid by the dividend-paying corporation as income taxes on its own profits (R. 25, 29, 33, 37, 41, 45, 53, 70).

Dividends upon stock in British corporations are not subject to tax at the standard rate when received by the shareholder,[18] but for purposes of the surtax imposed under Section 38 of the Fi-

[18] R. 116–117; Appendix A, Petitioner's Exhibit No. 1, pp. 14–15.

nance Act of 1927, *supra,* the shareholder is required to include in income not only the amount of cash received but also the amount certified as income tax "appropriate to" his dividend (R. 178). However, the fact that Great Britain requires the inclusion of this theoretical amount in the statement of income filed for surtax purposes does not make the amount income within the meaning of our statutes any more than are the amounts determined under Schedule A. Cf. *F. W. Woolworth Co.* v. *United States, supra.*

The taxpayer's contention that the amounts, certified as British and United Kingdom income taxes "appropriate to" the dividends received by him, represent taxes paid by deduction is based primarily upon the language of certain relief provisions found in the British law and the practice of British officials in administering those provisions.

The provisions relating to relief from income tax of earners of small income contain the following:

Section 29 of the Income Tax Act of 1918, *supra:*[14]

> (1) If it is proved to the satisfaction of the general commissioners that any person whose claim for exemption, abatement, or relief has been allowed, has paid any tax, by deduction or otherwise, the general commissioners may, in the form prescribed, certify

[14] R. 116–117; Appendix A, Petitioner's Exhibit No. 1, pp. 14–15.

the facts proved before them to the special commissioners.

(2) The certificate of the general commissioners shall state the particulars of the different sources of income in respect of which tax has been paid, the relief to which the claimant is entitled, the amount repayable in respect thereof, and the name and place of abode of the claimant.

(3) On receipt of the certificate, the special commissioners shall issue an order for repayment.

Section 32 of the Income Tax Act of 1918, *supra*:[15]

* * * * *

(2) If any such person is charged to tax under any Schedule and has paid that tax, or has paid or has been charged with tax by deduction or otherwise, he shall, on a claim being made to the special commissioners, and on production to them of the receipt for his annual payment, and proof of the facts to their satisfaction, be entitled to repayment of tax on the amount thereof.

Section 33 of the Income Tax Act of 1918, *supra*:[16]

(1) Where an assurance company carrying on life assurance business, or any company whose business consists mainly in the

[15] R. 117; Appendix A, Petitioner Exhibit No. 1, p. 17.

[16] R. 117–118; Appendix A, Petitioner's Exhibit No. 1, p. 19.

making of investments, and the principal part of whose income is derived therefrom, or any savings bank or other bank for savings, claims and proves to the satisfaction of the special commissioners that, for any year of assessment, it has been charged to tax by deduction or otherwise, and has not been charged in respect of its profits in accordance with the rules applicable to Case I, of Schedule D, the company or bank shall be entitled to repayment of so much of the tax paid by it as is equal to the amount of the tax on any sums disbursed as expenses of management (including commissions) for that year: * * *.

Section 27 of the Finance Act of 1920, 10 & 11 Geo. 5, c. 18:[17]

(1) If any person who has paid, by deduction or otherwise, or is liable to pay, United Kingdom income tax for any year of assessment on any part of his income proves to the satisfaction of the Special Commissioners that he has paid Dominion income tax for that year in respect of the same part of his income, he shall be entitled to relief from United Kingdom income tax paid or payable by him on that part of his income at a rate thereon to be determined as follows: * * *.

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[17] R. 118; Appendix A, Petitioner's Exhibit No. 3, p. 21.

(b) The amounts involved are not "taxes" within the meaning of applicable statutory provisions

The burden is upon the taxpayer to show that the amount claimed as a credit or deduction for taxes paid or accrued is the kind of an exaction for which a credit or deduction is authorized. Cf. *F. W. Woolworth Co.* v. *United States,* 91 F. (2d) 973 (C. C. A. 2d), No. 568, present Term; *Elgin National Watch Co.* v. *Commissioner,* 17 B. T. A. 339, 362; *Eitingon-Schild Co. and Subsidiaries* v. *Commissioner,* 21 B. T. A. 1163; *Mallouk* v. *Commissioner,* 34 B. T. A. 269; *Havana Electric Railway, Light & Power Co.* v. *Commissioner,* 34 B. T. A. 782.

The amount claimed as a credit in the instant case is not a "tax" within the meaning of the controlling provisions of our statutes. The word "tax" is generally understood in this country to mean an involuntary charge or enforced contribution of persons and property, levied exclusively by the legislative authority, for the support of the Government and for all public purposes. *Case of the State Freight Tax,* 15 Wall. 232, 278; *United States* v. *Railroad Co.,* 17 Wall. 322, 326; *Loan Association* v. *Topeka,* 20 Wall. 655, 664; *Florida Central &c. R'd Co.* v. *Reynolds,* 183 U. S. 471, 475; *Tevender* v. *Ruysdael,* 299 Fed. 746, 753 (C. C. A. 7th); *Pettibone* v. *Smith,* 150 Pa. 118, 126; *Perry* v. *Washburn,* 20 Cal. 318, 350; *Strand* v. *Marin,* 30 N. D. 165, 168–169. It is clear from the

record in this case that the amounts alleged to be British and United Kingdom income taxes "appropriate to" the dividends received by the taxpayer are not "taxes" as that term is generally understood in this country.

The record clearly shows that the amount treated by the British Government as income taxes "appropriate to" a dividend for purposes of the surtax and for relief purposes is not imposed as a tax by legislative authority. The amount is determined by reference to the tax rate in effect at the time of distribution and has no exact relation to any tax actually paid to the Crown. In *Neumann* v. *Commissioners of Inland Revenue,* 18 British Tax Cases 332, Lord Tomlin explained what this amount is (pp. 358–360):[18]

> The relative positions of a company and the shareholders of the company in relation to Income Tax under the Income Tax Acts have always been recognised as special in character. It was never, I think, doubted that under the Act of 1842, the profits of a business carried on by a company were taxable against the company under Schedule D, and were not taxable again, after distribution, in the hands of the shareholders under Schedule D or any other Schedule. At the same time, it was permissible to the company, under Section 54 of the Act of 1842,

[18] Printed in the record, pp. 297, 323–325. See, also, *Hamilton* v. *Commissioners of Inland Revenue,* 16 British Tax Cases 213, 233–234 (R. 265, 285–286).

to deduct from the dividend the proportionate part of the tax paid to the tax collector, and the shareholders entitled to exemption from or abatement of Income Tax could, upon the footing of the deduction, obtain the necessary return of tax. * * *

In practice, the matter did not work out quite so simply. It has to be remembered that the amount distributable in dividend in any year might, in view of the assessment of profits or gains under Schedule D being upon the basis of the average of the three preceding years, as it then was, be much more or much less than the amount of the assessment for that year, so that if this proportionate deduction was treated as meaning the rateable proportion of the tax paid by the company in respect of the year of distribution, it might much exceed or be much less than the amount which would be deducted from the dividend if the current rate of tax in respect of the gross dividend had been deducted. At any rate, a practice seems to have grown up of companies deducting from dividends tax appropriate to the amount of the dividend at the current rate of tax, quite irrespective of the amount of tax paid by the company to the Revenue, and of the shareholders claiming exemption or abatement being treated by the Revenue as having paid tax to the extent of that deduction. As the company making the deduction lay under no obligation to pay to the Revenue anything more than the tax based

> upon its own assessment, the result was that the tax returned to those claiming exemption or abatement could rarely, if ever, have had any exact relation to the amount of tax received by the Revenue from the recipient of returned tax.

The amount certified as tax "appropriate to" a dividend is not paid to the Crown, whether supposedly "deducted" from the dividend under Rule 20 or not, and it has no necessary relation to the amount which has been paid to the Crown by the corporation as a tax on the profits subsequently distributed as a dividend.[19]

In England the corporation income tax is regarded as being a disbursement out of profits and not an expense incurred in earning profits. Accordingly, a British corporation is entitled to declare a dividend in the amount of its entire profits without reduction on account of the tax it has paid. This is best understood by putting an example. A British corporation having a profit of £1,000 and paying an income tax thereon of £250 is entitled to declare a dividend of £1,000 (R. 125). But since the corporation in fact had only £750 to distribute, it is apparent that its dividend of £1,000 is a fiction. Therefore, although the company declares a dividend of £1,000 and designates £250 as the tax appropriate to the dividend, it is not in fact paying a dividend of £1,000 and making a "dedu-

[19] R. 147–148, 154–155, 163, 171–172, 184, and, particularly, 160.

tion" of £250. All of this, in a taxing system in which the corporation is taxed as a separate entity, is unreal and artificial, or, to use the word of the British expert, "constructive." (R. 179.) In the language of the expert (R. 172–173): "It is just one of the devices we are accustomed to employ to render the metaphysical more easily comprehended in a world of reality." It can be explained only as the survival of a system which had its origin a half century before the limited liability company became an effective organ (R. 137). It serves the purpose of enabling the British Government to charge the stockholder with the receipt of the gross dividend for surtax purposes, and thus require him to pay a tax upon income which he never received. It serves the further purpose of forming a basis for a refund to exempt taxpayers who pay no tax at all (R. 173). Both of these practices, of course, are only "constructive" when compared with the actual facts, for the taxpayer liable to surtax pays a tax on dividends he never received and the exempt taxpayer receives a refund for a tax he never paid, each in amounts which have no necessary relation to a proportionate part of the tax paid by the corporation. *F. W. Woolworth Co.* v. *United States, supra,* at p. 975. This is the basis upon which the stockholder is "regarded as a taxpayer." But it is clear that the term "taxpayer" applied to the recipient of the dividend is only one of convenience and is not founded upon actuality, be-

cause only one tax is collected, and that from the corporation (R. 176–177). We submit that the right to a credit under the Federal Revenue Acts depends upon whether the claimant has *actually paid* a tax, and not upon the designation applied to him by a foreign government.

The expert testified that if a company does not declare a dividend out of its profits the company is left to bear the tax and its only way of recovery from its shareholders is to pay a dividend and pass the tax on (R. 126), thus recouping itself only if it pays the dividend (R. 127). This Court has held that an amount passed on as a tax is not a tax in reality. *Lash's Products Co.* v. *United States,* 278 U. S. 175. There it said (p. 176): "The phrase 'passed the tax on' is inaccurate, as obviously the tax is laid and remains on the manufacturer and on him alone." Since the British corporation is only permitted and not required to make the so-called "deduction" from its dividends, it is clear that the so-called passing on of the tax is entirely a corporate action and not the exertion by the sovereign of the taxing power. The only tax which finds its way into the coffers of the Crown is the tax paid by the corporation upon its own profits (R. 163, 173). The expert testified that only a sum paid to the Crown was regarded as a tax (R. 154), but he was unable to answer the question as to whom the sum "deducted" from the dividend was

paid and said that question has never arisen in England (R. 162).

The corporation itself keeps the tax "appropriate to the dividend" (R. 128). It does not turn over that sum to the Crown, because it has already paid its own tax (R. 141). This makes it abundantly clear that the only tax collected is from the corporation on its own account and not as agent of the stockholders (R. 134, 146). The question never arises whether, or to what extent, the corporation has accounted to the Crown for its tax. The whole point is that the dividend-paying company, acting under statutory authority, has made a deduction from the shareholders (R. 155). Moreover, the so-called "deduction" is made at the rate of tax applicable to the year of the dividend, which may be more or less than the rate applicable to the tax paid by the corporation upon its own profits, for that tax may have been paid in a previous year at a different rate, as fully explained in the quotation above, pp. 26–27, from the *Neumann* case. Therefore, there is not even a precise relationship between the amount actually paid as tax by the corporation and the so-called "deduction" (R. 160, 161, 184).

Clearly, the amount in controversy does not represent "taxes" of any kind in the sense in which that term is used in Section 23 (c) and 131 (a) of the Revenue Act of 1928.

(c) *The Amount in Controversy Has Not Been "Paid" to a Foreign Country, Either by the Taxpayer or by Any One Acting on His Behalf*

The opinion of the court below is predicated upon a misstatement of fact together with references to the British law which do not support its factual conclusions. It is first stated that the taxpayer, by reason of his stock holdings in British companies, received the net amount of $23,993.72 as dividends, "such dividends being accompanied by certification that $7,017.11 had been deducted and paid directly to the British Government" (R. 387). The certificates accompanying the taxpayer's dividend warrants made no such statement (R. 25–67), and nowhere in the record does it appear that the amount certified as income taxes "appropriate to" the dividends received was "paid directly to the British Government." Furthermore, it does not appear that this particular amount was "paid" to the British Government by either the taxpayer or by the corporations paying the dividends.

The court below conceives the question to be whether the amount certified as income tax "appropriate to" the dividends was a tax "directly borne by the petitioner, or was it a tax imposed upon and borne by the British companies?" (R. 388.) Whether the taxpayer bore the ultimate burden of an income tax imposed by Great Britain is not the question. The question is whether the taxpayer "paid" this amount as the term is used

in the sections authorizing the credit and deduction for taxes paid. No doubt a shareholder in a British corporation bears his proportionate share of the ultimate burden of a tax imposed upon the corporation, just as a shareholder in a corporation subject to tax in this country ultimately bears his share of the burden of our taxes through a reduction of corporate profits which otherwise would be available for distribution to him as dividends. This condition, however, results from his relationship to the corporation because of his stockholding and not because of any tax imposed upon him, either directly or indirectly.

Our courts, the Board of Tax Appeals, and the Treasury Department have refused to accept the principle of "ultimate burden" of taxation, and have consistently held that only such taxes as are imposed upon and paid by the taxpayer can be deducted from gross income in computing its taxable net income. That was the conclusion of the Circuit Court of Appeals for the Second Circuit in *Biddle* v. *Commissioner,* 86 F. (2d) 718, 720, which was a companion to the instant case before the Board and which is now before this Court, No. 55, present term. See also *Helvering* v. *Missouri State Life Ins. Co.,* 78 F. (2d) 778 (C. C. A. 8th); *Falk Corporation* v. *Commissioner,* 60 F. (2d) 204 (C. C. A. 7th); *Colston* v. *Burnet,* 59 F. (2d) 867 (App. D. C.), certiorari denied, 287 U. S. 640; *Robinson* v. *Commissioner,* 53 F. (2d) 810 (C. C. A. 8th);

National Piano Mfg. Co. v. *Burnet,* 50 F. (2d) 310 (App. D. C.); *Shearer* v. *Commissioner,* 48 F. (2d) 552 (C. C. A. 2d); *Perry* v. *Commissioner,* 32 B. T. A. 513; *California Sanitary Co.* v. *Commissioner,* 32 B. T. A. 122; *Peterson* v. *Commissioner,* 31 B. T. A. 172; *O'Neil* v. *Commissioner,* 31 B. T. A. 727; *Small* v. *Commissioner,* 27 B. T. A. 1219; *Hamilton* v. *Commissioner,* 6 B. T. A. 240; *Musser* v. *Commissioner,* 3 B. T. A. 498; A. R. R. 1020, I–2 Cumulative Bulletin 104; S. M. 3714, IV–2 Cumulative Bulletin 50; I. T. 2768, XIII–1 Cumulative Bulletin 54; I. T. 2783, XIII–1 Cumulative Bulletin 54; I. T. 2790, XIII–1 Cumulative Bulletin 56; I. T. 2787, XIII–1 Cumulative Bulletin 56. There is no apparent reason why a different rule should apply in the case of a credit for foreign taxes.

The sum of $7,017.11 was not imposed upon the taxpayer as a tax and was not "paid" by him as a tax within the meaning of our statutes. The testimony of the expert witness clearly shows that only one normal tax at the "standard" rate upon income is imposed and collected by the Crown (R. 124, 178); that that tax is imposed upon the company as a tax upon its trading profits (R. 127, 141, 150–151, 153, 159, 165, 172); that there is no tax at the normal or "standard" rate imposed upon stockholders with respect to dividends received from British corporations (R. 137–138, 150); that a British corporation does not pay its own tax as an agent for the shareholders (R. 134, 146, 172–173); and

that the company does not act as a collector for the Crown when it purports to deduct from a dividend an amount alleged to be taxes "appropriate to" the dividend paid (R. 127, 141, 172, 177, 184). The witness' interpretation of the English law is fully supported by the decisions of the English courts. See *Ritson* v. *Phillips,* 9 British Tax Cases 10; *Purdie* v. *The King,* 3 K. B. [1914] 112; *Neumann* v. *Commissioners of Inland Revenue, supra; Bradbury* v. *English Sewing Cotton Co., Ltd.,* 8 British Tax Cases 481; *Commissioners of Inland Revenue* v. *Dalgety & Co.,* 15 British Tax Cases 216; *Scottish Union & National Insurance Co.* v. *New Zealand and Australian Land Co.,* 1 L. R. App. Cas. [1921] 172; *Sheldrick* v. *South African Breweries, Lt.,* 1 K. B. [1923] 173; *Commissioners of Inland Revenue* v. *Blott,* 8 British Tax Cases 101; *Hamilton* v. *Commissioners of Inland Revenue, supra.* (The *Neumann, Dalgety,* and *Hamilton* cases are printed in the record, pages 297, 341, and 265, respectively.)

In *Ritson* v. *Phillips, supra,* Justice Rowlatt said of a shareholder (p. 14):

> He is not taxed on his dividends. The companies are taxed on their profits, not as his agents (as has been loosely said), though at his ultimate expense. There is no provision for the return of any of this tax to the shareholder save in the process of giving effect to deductions and reliefs.

In *Purdie* v. *The King, supra,* the same Justice stated (pp. 116–117):

> * * * Sched. D charges income tax upon the profits of the company made on behalf of its shareholders; and s. 54 of the Income Tax Act, 1842, provides that every company shall deliver a true statement of its annual profits before any dividend has been made to any persons and that such persons shall allow out of the dividends a proportionate deduction in respect of the duty charged. The company, therefore, is assessed and pays the tax. There is, strictly speaking, no tax upon dividends at all; the company has to pay income tax upon its profits as a company, and, having paid the income tax, the effect is that there is less to divide among the shareholders. Sometimes a company declares what it calls a dividend "free of income tax," which means that having paid income tax the dividend paid is less because there is less to divide. Sometimes it declares a dividend which it does not call free of income tax, and then it deducts a certain percentage from the dividend, stating that it is for income tax. The real effect of the latter course is, not that the company has declared a dividend of the full amount and then deducted income tax from it, but that it has declared a dividend of the net amount and told the shareholders that it would have been so much more but for the fact that the profits of the company were charged with income tax before the dividend was made.

In approving the above statement Lord Tomlin said in *Neumann* v. *Commissioners of Inland Revenue, supra,* a case arising under the Income Tax Act of 1918 (p. 362, R. 327):

> I may say at once that, having regard to the view which I have expressed as to the general scheme and operation of the Income Tax Acts in regard to dividends, I am unable to accept the view that dividends, as such, are taxable under Schedule D. I do not think they are.

In *Sheldrick* v. *South African Breweries, supra,* a case dealing with the deduction by the company of British income taxes "appropriate to" dividends on preferred stock, Lord Warrington said (pp. 186–187):

> In the case of a company it is the company which directly pays the tax upon its profits. The shareholders bear their due proportion of the tax by a power given to the company by r. 20, which I will read directly, of deducting the due proportion of the tax from the dividends which the company pays. And accordingly for the purpose of s. 43 it is the company and not the shareholders of the company who is the person who has paid the income tax and is entitled to relief.

The same view was stated in unmistakable language in *Bradbury* v. *English Sewing Cotton Co., supra.* There, the taxpayer was an English company which owned all of the stock of an American company. During the years 1914 to 1919, inclusive, it received dividends from the American company.

During the years 1914 to 1916, inclusive, the English courts held the American company to be a resident of Great Britain, though incorporated and doing all its business in the United States, and held it subject to tax under the British laws. Control of the American company was transferred to the United States in 1917, and it was conceded not to be taxable under British law for the years 1917 to 1919, inclusive, the years involved in that litigation. During all of the years 1914 to 1919, inclusive, the British income tax was, under the statutes, computed upon the average of the company's earnings for the preceding three years. The Crown contended that the dividends received by the British company from the American company during 1917, 1918, and 1919 should be included in computing the average income of the British company for the three preceding years upon which the tax for those years was to be computed. The House of Lords held that the dividends received from the American company prior to the time control was transferred to the United States had already borne their tax burden and could not be included in the computation of income upon which the tax for subsequent years was to be determined. In the course of his judgment Lord Wrenbury said (p. 516): [20]

> The English Sewing Cotton Company during the first three years held, and they

[20] To the same effect was Lord Phillimore's statement in the same case, pp. 518–520.

subsequently continued to hold, all, or nearly all, the ordinary shares in the American Company. They were entitled to receive, and did receive, dividends in respect of them. The fund available for their payment was not the profits of the American Company, but the differential sum remaining after deduction from those profits of the Income Tax which the American Company was liable to pay and had paid. And the person to make payment to them was the American Company. The case was one within Section 52 of the Income Tax Act, 1842. The English Company as a holder of shares in the American Company was a person to whom an annual payment was made out of property of the American Company in respect of which the American Company was chargeable to Income Tax under the Act. The English Company could not, during the first three years, be assessed, and was not assessed, in respect of the dividends thus received. The American Company was the person, and the only person who could be assessed in respect of the profits of the business of the American Company. The corporator bore his share of the tax by the deduction of the appropriate share of the collective tax paid by the corporation from his dividend (*Inland Revenue* v. *Blott,* [1920] 1 K. B. 114, 130, 131).

In *Commissioners of Inland Revenue* v. *Blott,* 8 British Tax Cases 101, and *Commissioners of Inland Revenue* v. *Greenwood,* decided with it, two

corporations capitalized their accumulated profits and issued stock dividends to their shareholders. The question involved in both cases was whether the value of shares received as stock dividends should be included in computing income subject to Super-Tax under the Finance Act of 1910. It was held that the stock dividends did not constitute income to the shareholders, but in the course of his opinion Viscount Cave said (pp. 135–136):

> Some time was occupied in the discussion of the question, whether in paying Income Tax on its profits the Company acted as agent for its shareholders, and some cases were cited where this expression had been used. Probably the word was intended only to express in an abbreviated form the effect of Section 54 of the Income Tax Act, 1842. Plainly, a company paying Income Tax on its profits, does not pay it as agent for its shareholders. It pays as a taxpayer, and if no dividend is declared the shareholders have no direct concern in the payment. If a dividend is declared, the company is entitled to deduct from such dividend a proportionate part of the amount of the tax previously paid by the company; and, in that case, the payment by the company operates in relief of the shareholder. But no agency, properly so-called, is involved.

Since the above decision in the *Blott* case it seems to be clear that a corporation pays its tax on its own behalf and does not pay as agent of the stock-

holders. See *Sheldrick* v. *South African Breweries, supra,* pp. 191–193; *Ritson* v. *Phillips, supra,* p. 14; *Scottish Union & National Insurance Co.* v. *New Zealand & Australian Land Co., supra,* pp. 184–187; *Commissioners of Inland Revenue* v. *Dalgety & Co., supra,* pp. 230–232 (R. 355–357); *Hamilton* v. *Commissioners of Inland Revenue, supra,* pp. 230–232 (R. 282–284). The company does not, in certifying the amount of income tax "appropriate to" a dividend, act as a collector for the Crown, as it would in the case of a deduction made under Rules 19 and 21 of the General Rules applicable to all Schedules.[21] Cf. *Hamilton* v. *Commissioners of Inland Revenue, supra,* pp. 228–230 (R. 280–282); *Commissioners of Inland Revenue* v. *Dalgety & Co., supra,* pp. 231–232 (R. 356–357); *Neumann* v. *Commissioners of Inland Revenue, supra,* p. 368 (R. 333).

If it can properly be said that common shareholders suffer anything by way of deduction from their dividends, the amount deducted merely goes to recoup the company for amounts paid to discharge its own liability. (R. 127, 177). It does not constitute a payment of tax to the Crown by the shareholder. This is particularly emphasized by the decision in the *Dalgety* case, *supra.* There, the taxpayer was a British corporation doing most of its business in Australia and New Zealand. It

[21] Record, Appendix A, Petitioner's Exhibit No. 1, pp. 198, 199.

had a small amount of income from sources within Great Britain on which it paid income tax. It had a far larger amount of income from sources within Australia and New Zealand which was subject both to United Kingdom income tax and Dominion income taxes. The British statutes provided certain reliefs from United Kingdom income taxes in such cases where the income was also subject to Dominion income taxes. It was admitted in the *Dalgety* case that the company was entitled to relief, the only question being the amount of relief to which it was entitled. The controversy arose because the company had outstanding a large bond issue bearing a fixed rate of interest. In paying the interest on its debentures the company deducted, under Rule 19 of the General Rules applicable to all Schedules,[22] the amount of United Kingdom income tax applicable to such interest payments. The income from sources within Great Britain was insufficient to pay all of this interest, with the result that Dominion income was used in paying the balance. In computing the relief allowed to the company the revenue officials refused to allow relief from United Kingdom income tax on that part of the Dominion income used in paying the interest, basing their refusal upon the ground that the company was able to recoup that part of the United Kingdom income tax applicable to Dominion income used to pay interest. See Lord Mac-

[22] Record, Appendix A, Petitioner's Exhibit No. 1, p. 198.

millan's statement of the Crown's contention, p. 253 (R. 378). The Court of Appeals and the House of Lords, reversing the King's Bench, held that the company paid United Kingdom and Dominion income taxes on this income, and under a proper interpretation of the relief provisions involved was entitled to full relief although it had not actually borne the burden of the tax to the exent that interest payments were reduced.

While the decision in the *Dalgety* case is right, at least in so far as our concept of taxation is concerned, it produces an anomalous result. The company was granted the relief afforded a *taxpayer* by the British statutes, yet under certain provisions of the British law for the accordance of relief, which we have cited above, the debenture holders would be entitled to refunds from the Crown if their ultimate income tax liability did not equal the amount deducted from their interest payments. Yet it is clear from the record in the instant case that there is but one tax at the "standard" rate collected by the Crown; there is but one taxpayer which pays the tax to the Crown; and as between the corporation and its shareholders the tax is imposed upon and paid by the corporation as its tax. Those relief provisions are administered on the theory that a corporate shareholder has paid an amount equal to the amount certified as income tax "appropriate to" his dividend. But this does

not, we submit, make the shareholder a taxpayer with respect to that amount in so far as our taxing statutes are concerned.

The taxpayer's expert witness testified that in his twenty years of experience the precise question here involved had never arisen and he doubted whether it could arise under British law. Consequently, the British cases are helpful only to the extent that they show how the British law operates in actual administration. We do not believe those cases establish any British interpretation which holds the shareholder liable as the taxpayer for income taxes assessed upon the income of the corporation.

The court below placed too much reliance upon the testimony of the expert witness to the effect that under British law "the shareholder is regarded as a taxpayer in respect to the amounts deducted from the dividends for income taxes 'appropriate' thereto" (R. 389). The question here is not whether the British law "regards" the shareholder as a taxpayer, but whether he "paid" a tax in the sense in which the term is used in the Federal Revenue Acts. While foreign law is a question of fact, to be proven as any other fact, the construction and effect of the foreign law is a question of law for the court to decide. *Bank of China* v. *Morse*, 168 N. Y. 458, 469–470; *Hanna* v. *Lichtenhein*, 225 N. Y. 579, 582–583; *Minero* v. *Ross and*

Masterson, 106 Tex. 522, 535–536. In *Hanna* v. *Lichtenhein, supra,* the court said (pp. 582–583):

> Foreign law is a question of fact and must be proved as such, but when after such proof is given the questions involved depend upon the construction and effect of a statute or judicial opinion they are for the court and not questions of fact at all.

This is clearly the true rule, supported by the great weight of authority. *Fitzpatrick* v. *International Ry. Co.,* 252 N. Y. 127, 136–137, annotated, 68 A. L. R. 809. While there appears to be some divergence of view in the state courts, the rule stated is clearly the law in the Federal courts. *Eastern Building &c. Assn.* v. *Williamson,* 189 U. S. 122, 126–127; *Finney* v. *Guy,* 189 U. S. 335, 342; *Scheer* v. *Rockne Motors Corp.,* 68 F. (2d) 942, 945 (C. C. A. 2d).

Here the decisions of the British courts were introduced in evidence, and hence it was the duty of the court to determine for itself what those decisions held. However, if it can be said that the British law regards the shareholder as the taxpayer rather than the person who bore the ultimate burden of the corporation's income tax liability, it is plain that he is regarded as such only for the purpose of administering the relief provisions already referred to and for the purpose of requiring the inclusion in gross income, for purposes of the surtax, of the amount of net dividend received plus income tax "appropriate thereto."

The fact that British law requires the inclusion of this amount in gross income, or that it takes this amount into consideration in administering its relief provisions, is not determinative of the question involved here. This Court pointed out in *Merchants L. & T. Co.* v. *Smietanka,* 255 U. S. 509, 521–522, that the British taxing acts are quite different from our acts.

The British concept of income differs from ours and any inferences drawn from the fact that under British law an item is treated as income would be misleading in the determination of the status of the same item as income under our law. As pointed out by the Circuit Court of Appeals for the Second Circuit in the *Woolworth* case, *supra,* the British shareholder must compute his super-tax upon a nominal dividend which he never receives. Such a practice finds no counterpart in our law and it is futile to attempt to rationalize it with our tax system and constitutional limitations.

The court below gives several other reasons to support its conclusion, each of which is untenable. The first is that the British law is based upon the principle of collection at the source (R. 389). But the record clearly discloses that the amount here involved was not a tax collected at the source and paid to the Crown. It was merely an amount which had some inexact relation to a tax earlier imposed on and paid by the corporation. Another reason given is that British corporations are bound by

law to show not only the net amount of dividends actually paid but also a constructive gross amount of dividends and the income tax appropriate thereto (R. 389). This, again, does not mean that the amount certified as "appropriate to" the dividend represents a tax liability of the shareholder which has been or will be paid to the Crown. The certificates themselves clearly negative any such notion. As already shown, the language of the relief provisions cited (R. 390) do not support the conclusion of the court.

Among other things, the court relies upon the legal principle that if there is any doubt in the construction of a taxing statute that doubt is to be resolved in favor of the taxpayer. (R. 391.) But an examination of Section 131 (a) and Section 23 (c) of the 1928 Act will show that they are entirely clear and not relief provisions as suggested by the court (R. 390–391). Instead, they are provisions allowing credits and deductions, and the taxpayer claiming a credit or deduction must bring himself within those provisions.

II

PRIOR PRACTICE OF THE BUREAU OF INTERNAL REVENUE IS NOT BINDING ON THIS COURT

It is true, as pointed out by the court below (R. 392), that the Bureau of Internal Revenue formerly allowed such credits. However, that practice is not binding upon the courts for two reasons.

In the first place the rulings referred to are not in any sense an interpretation of our statutes. A cursory examination of these rulings leaves no doubt of their substance. They decide, erroneously we think, that the tax appropriate to a dividend is a real exaction imposed upon stockholders and actually paid into the British Treasury. In other words, they are an interpretation of the British statutes.

In S. M. 3040, IV–1 Cumulative Bulletin 198, it appears that the Treasury believed that the tax paid by the corporation with respect to its earnings and profits was a tax paid as agent of the stockholders, since the corporation was permitted to deduct, upon the payment of dividends, a tax appropriate to the dividends. However, in S. M. 5363, V–1 Cumulative Bulletin 89, although the decision in S. M. 3040 was sustained, the Treasury ruled that the tax on the corporate profits which are retained is a tax upon the corporation, but that the tax on the profits distributed is a tax upon the stockholders. This decision was reaffirmed in I. T. 2401, VII–1 Cumulative Bulletin 126.

Since respondent does not claim the credit here upon the *reasoning* of these decisions they would seem to be wholly inapplicable. Respondent does not contend that the British corporation pays its own income tax as agent for its shareholders, and it is clear that it does not (R. 284). Neither does respondent claim that the tax paid by the corpora-

tion upon the portion of its profits distributed as dividends is a tax paid by the corporation on behalf of the stockholders. The testimony of respondent's expert makes it clear there is no room for such a contention (R. 140–141). Respondent cannot rely merely upon the decision contained in the Treasury rulings and abandon the reasoning upon which those rulings are based. Respondent cannot be heard to say that although the reasoning has been demonstrated to be erroneous the decision remains in effect.

While the reasoning of those decisions has been shown to be erroneous, respondent could not rely upon the reasoning even if it were correct, for he has failed to prove the year or years in which the British corporations from which he received his dividends paid their income tax.

The record does not disclose the year or years in which the profits distributed as dividends in 1931 were taxed. If the 1931 dividends represent corporate profits earned and taxed in a prior year, the respondent is not entitled to credit the tax against his 1931 income. In other words, the year in which the tax is paid to the British Government is the year in which the credit must be taken and it is not sufficient for respondent to show merely that a tax was paid for him by the corporation at some undisclosed time.

Another reason why the Bureau practice is not controlling is well illustrated by this Court in

Burnet v. *Chicago Portrait Co.*, 285 U. S. 1, where after stating (p. 16), "The court is not bound by an administrative construction" contained in regulations under the several Acts, it concluded that (p. 21):

> The decisions of the Treasury Department applying these regulations have no more force than the reasons given to sustain them and these, in our opinion, furnish no adequate ground for denying effect to the credit provisions of the statute in accordance with their manifest purpose.

The courts have never hesitated to overrule regulations of the Treasury Department if they are contrary to law or not supported by the law. And where, as here, the law is plain the doctrine of adoption of departmental construction by subsequent reenactment does not apply. *Biddle* v. *Commissioner*, 86 F. (2d) 718, 721 (C. C. A. 2d), No. 55, present Term, and cases there cited; see *Hamilton* v. *Rathbone*, 175 U. S. 414, 419; *Thompson* v. *United States*, 246 U. S. 547, 551; *United States* v. *Hartwell*, 6 Wall. 385, 396; *Helvering* v. *N. Y. Trust Co.*, 292 U. S. 455.

Furthermore, an erroneous interpretation of the statute by the Commissioner of Internal Revenue does not conclude the courts after a subsequent modification of the ruling and does not create equities in favor of the taxpayer requiring a judicial adoption of the erroneous interpretation. Cf. *American-La France Fire Engine Co.* v. *Riordan*,

294 Fed. 567, 572 (W. D. N. Y.); *Langstaff* v. *Lucas*, 9 F. (2d) 691, 693 (W. D. Ky.), affirmed, 13 F. (2d) 1022 (C. C. A. 6th), certiorari denied, 273 U. S. 721.

CONCLUSION

The decision of the court below is erroneous and should be reversed.

Respectfully submitted.

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APPENDIX

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 22. GROSS INCOME.

(a) *General definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

* * * * *

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(c) *Taxes generally.*—Taxes paid or accrued within the taxable year, except—

(1) income, war-profits, and excess-profits taxes imposed by the authority of the United States;

(2) so much of the income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States as is allowed as a credit against the tax under section 131; and

(3) taxes assessed against local benefits of a kind tending to increase the value of the property assessed; but this paragraph shall not exclude the allowance as a deduction of so much of such taxes as is properly allocable to maintenance or interest charges.

For the purpose of this subsection, estate, inheritance, legacy, and succession taxes accrue on the due date thereof, except as otherwise provided by the law of the jurisdiction imposing such taxes, and shall be allowed as a deduction only to the estate.

* * * * *

SEC. 115. DISTRIBUTIONS BY CORPORATIONS.

(a) *Definition of dividend.*—The term "dividend" when used in this title (except in section 203 (a) (4) and section 208 (c) (1), relating to insurance companies) means any distribution made by a corporation to its shareholders, whether in money or in other property, out of its earnings or profits accumulated after February 28, 1913.

* * * * *

SEC. 131. TAXES OF FOREIGN COUNTRIES AND POSSESSIONS OF UNITED STATES.

(a) *Allowance of credit.*—The tax imposed by this title shall be credited with—

(1) CITIZEN AND DOMESTIC CORPORATION.—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, and excess-profits taxes paid or accrued during the taxable year to any foreign country or to any possession of the United States; and

(2) RESIDENT OF UNITED STATES.—In the case of a resident of the United

States, the amount of any such taxes paid or accrued during the taxable year to any possession of the United States; and

(3) ALIEN RESIDENT OF UNITED STATES.—In the case of an alien resident of the United States, the amount of any such taxes paid or accrued during the taxable year to any foreign country, if the foreign country of which such alien resident is a citizen or subject, in imposing such taxes, allows a similar credit to citizens of the United States residing in such country; and

(4) PARTNERSHIPS AND ESTATES.—In the case of any such individual who is a member of a partnership or a beneficiary of an estate or trust, his proportionate share of such taxes of the partnership or the estate or trust paid or accrued during the taxable year to a foreign country or to any possession of the United States, as the case may be.

(b) *Limit on credit.*—In no case shall the amount of credit taken under this section exceed the same proportion of the tax (computed on the basis of the taxpayer's net income without the deduction of any income, war-profits, or excess-profits tax any part of which may be allowed to him as a credit by this section), against which such credit is taken, which the taxpayer's net income (computed without the deduction of any such income, war-profits, or excess-profits tax) from sources without the United States bears to his entire net income (computed without such deduction) for the same taxable year.

* * * * *

(e) *Proof of credits.*—These credits shall be allowed only if the taxpayer furnishes evidence satisfactory to the Commissioner showing the amount of income derived from sources without the United States, and all other information necessary for the verification and computation of such credits.

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